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June 20, 2006

AGENDA ITEM 14

TO: MEMBERS OF THE HEALTH BENEFITS COMMITTEE

I. SUBJECT: First Reading: Long-Term Care Program 2005 and Earlier Rates − Proposed Mitigation Strategies

II. PROGRAM: Health Program

III. RECOMMENDATION: Information Only

IV. ANALYSIS:

Staff and the Long-Term Care Advisory Committee (Committee) met on June 6, 2006, to continue discussions regarding appropriate responses to the deficit position for the Long-Term Care Program (Program). Staff, at the direction of the Health Benefits Committee, had prepared and distributed to the Committee members and CalPERS Board members prior to the meeting a mitigation strategy that includes rate increases on all policies in-force and other actions (Attachment 1). The distribution also included a letter from United Health Actuarial Services (Attachment 2) providing analysis and recommendations prepared by the Program's consulting actuary in support of the staff proposal.

The staff proposal was based on the following assumptions:

- CalPERS does not have the ability to subsidize this Program with other business lines or financial reserves as does other long-term care insurance carriers.

- The Program began at a point in time where the long-term care insurance marketplace was relatively new and volatile.

- The long-term care marketplace has matured with many insurers leaving the market; the ones that remain, or are entering the market, are savvier and more financially stable.

- In recent years, new policy sales for this Program have been low but generally better than in the individual long-term care marketplace. New policies have balanced departures with total policies in-force remaining basically flat. Based upon this, the Program cannot look to expand to cover the projected deficit.

- The CalPERS Board has approved two concepts to change the focus of the Program: 1) build reserves and no longer have a "break-even" Program, and 2) do not continue to cross subsidize across products.
- In order for CalPERS to compete on a level field with commercial carriers, it would require a segmentation of the current risk pool through two-party discounts (spousal), prime, average, and sub-average rates and other discounts and incentives linked to more restrictive underwriting.
- An expansion of market penetration (new sales), would require a substantial commitment of additional assets including a real sales force (an agent network) as opposed to the marketing currently undertaken by the Program.

Staff Recommendation

Based on the history of the Program and the facts uncovered through in-depth research and discussion, staff and Karl Volkmar, Actuarial Consultant, United Health Actuarial Services, Inc., recommend that the Program focus on ensuring there are adequate reserves to meet the demands of current in-force policies. Staff and the Consultant propose a premium rate increase for all 2005 and prior policies which would be self-sufficient within each individual product cell to support the development of a comprehensive mitigation plan. The proposed rate increase is based upon the 2006 rates or 20% increase, whichever is less, with the exception of "lifetime" policies which will be increased to an appropriate pricing level. This increase is to be adequate enough to build reserves with no cross subsidization for either plan design or age group. This proposal builds reserves without placing an additional cost burden or disincentives for younger or newer policy holders. With this rate increase, members will be allowed a one-time opportunity to choose between two options as an alternative to the rate increase:

1) The member can step back to a lower Daily Benefit Allowance (DBA), (with a waiver of the underwriting requirements and utilization of their age at issuance into the Program).

2) The member can step back from the "lifetime" policy to a six-year (or shorter) term policy (with a waiver of the underwriting requirements and utilization of their age at issuance into the Program).

Claims experience for this program and broader industry information indicate that for most members a lifetime policy represents an unnecessary cost and over-insurance. Overall, the implementation of this rate increase will bring in-force premium rates in-line with 2006 rate levels.

Staff further recommends that this premium increase become effective on February 1, 2007, or the next available billing date for those members that are not billed on a monthly basis.

The Committee requested that the Program's consulting actuary provide rate increase scenarios based on the following assumptions:

- A 3 percent reserve margin for all in-force policies (retaining a 10 percent margin for new policies).
- Spreading of rate increases across 1 through 5 years.
- Continuation of the age adjustment (socialization) of a rate increase used for the 2003 rate increase.
- The age adjustment should be modified to narrow the range of adjustment and provide a higher minimum rate increase than occurred in 2003.

The Committee is scheduled to meet again in July to discuss the results of the above analysis. Staff will present the outcomes of those discussions and recommendation for mitigation strategies as an action item at the August 15, 2006, Health Benefits Committee meeting.

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Richard J. Krolak, Chief
Office of Health Plan Administration

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Terri Westbrook
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Attachments